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UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF CALIFORNIA
FRESNO DIVISION

In re) Case No. 24-11015-B-11
)
PINNACLE FOODS OF CALIFORNIA LLC,) Docket Control No. KCO-4
)
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Debtor.)
)
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_____)

MEMORANDUM ON DEBTOR'S MOTION TO ASSUME FRANCHISE AGREEMENTS

Michael J. Berger, Law Offices of Michael J. Berger, Beverly Hills, CA, for Pinnacle Foods of California, LLC, Keith C. Owens, Craig R. Tractenberg, FOX ROTHSCILD LLP, for Pinnacle Foods of California LLC, Movant/Debtor.

Glenn D. Moses, VENABLE, LLP, for Popeyes Louisiana Kitchen, Inc., franchisor.

Walter R. Dahl, Subchapter V Trustee.

RENÉ LASTRETO II, Bankruptcy Judge:

INTRODUCTION

This case presents a collision between the Bankruptcy Code (11 U.S.C. § 101 et seq.), the Lanham Act (15 U.S.C. §§ 1051 et seq.), and California's Franchise Relation Act ("CFRA") (Cal. Bus. & Prof. Code §§ 2000 et seq.). The fallout is a franchisor's hypothetical lack of consent and 11 U.S.C. § 365(c)(1) leave a franchisee-debtor with restricted pathways to reorganization in the Ninth Circuit.

1 Pinnacle Foods of California, LLC, Debtor and Debtor-in-
2 Possession("DIP") in the above-styled Chapter 11, Subchapter V
3 case (the "Debtor" or "Pinnacle"), moves for an order authorizing
4 Debtor to assume six separate franchise agreements (collectively
5 "the Franchise Agreements") with franchisor Popeyes Louisiana
6 Kitchen Inc. ("Popeyes"). Doc. #226. Popeyes vigorously opposes
7 assumption, and Pinnacle has replied. (Doc. #245 and #260).
8

9 I.

10 A.

11 Pinnacle is a franchisee of Popeyes which owns and operates
12 a network of six Popeyes fast food restaurants. Five in Fresno,
13 California and one in Turlock, California under the auspices of
14 the Franchise Agreements. Doc. #228 (Declaration of Imran
15 Damani). Imran Damani ("Damani") is the owner of Pinnacle and
16 two related entities, Tyco Group LLC ("Tyco") and California QSR
17 Management Inc. ("California QSR"), both of which are also
18 debtor-corporations in separate Chapter 11 Subchapter V cases,
19 but which are not implicated directly in the instant motion. Id.
20 Collectively, Pinnacle and Tyco will be referred to as "the
21 Franchisee Debtors" and all three entities will be referred to as
22 "the three Debtors." According to Damani's Declaration,
23 Pinnacle's Chapter 11 plan and this motion to assume the
24 Franchise Agreements provide for a prompt cure of any prepetition
25 defaults and adequate assurances of future performance based on
26 the ability of the three Debtors to reorganize. Id. Popeyes has
27 a contrary view.

28 ///

1 Popeyes has responded to Pinnacle's motion to assume arguing
2 that notwithstanding the relevant provisions of 11 U.S.C. § 365,
3 Pinnacle cannot assume the Franchise Agreements without Popeyes'
4 consent, and such consent will not be given. Doc. #245. Popeyes
5 relies on § 365(c)(1) which, as interpreted in the Ninth Circuit,
6 states that Popeyes' is excused from accepting performance or
7 rendering performance to a hypothetical third party. Id. Because
8 Pinnacle cannot assign the Franchise Agreements without Popeyes'
9 consent due to the operation of certain provisions of both the
10 Lanham Act and the 2015 amendments to CFRA, Pinnacle is also
11 barred from assuming the Franchise Agreements. Id. This argument
12 is derived from a legal concept indigenous to bankruptcy
13 assignment and assumption issues known as "the hypothetical third
14 party test" (or "the hypothetical test"), adopted by the Ninth
15 Circuit in *Catapult Entertainment, Inc. v. Perlman (In Re*
16 *Catapult Enter.)*, 165 F.3d 747 (9th Cir., 1999) and discussed
17 more in depth below.

18 As alternative grounds for denying the motion, Popeyes
19 asserts that Pinnacle has committed incurable non-monetary
20 defaults under the Franchise Agreements and has failed to cure
21 undisputed monetary defaults, and thus, the motion to assume must
22 be denied. Id. Pinnacle disputes that there is a non-monetary
23 default at all. Pinnacle also contends it need not cure all
24 monetary defaults.

25 In reply, Pinnacle presents arguments that CFRA contains
26 provisions which defeat Popeyes' arguments under the hypothetical
27 test. Doc. #260. Pinnacle also argues that it is in the process
28 ///

1 of curing the various monetary defaults. Id. Pinnacle's reply
2 brief does not address Popeyes' Lanham Act arguments.

3 The instant motion and the opposition go to the very heart
4 of this case. If Pinnacle cannot assume the Franchise
5 Agreements, there is essentially no business left to reorganize,
6 except perhaps by a sale of the franchises. Thus, the court will
7 address the threshold legal issue, the *Catapult* test. The
8 parties have submitted their briefs and on October 8, 2024, the
9 court heard arguments on this motion and took the matter under
10 advisement.

11
12 B.

13 The United States District Court for the Eastern District of
14 California has jurisdiction of this matter under 11 U.S.C.
15 § 1334(b) and referred this matter to this court under 28 U.S.C
16 § 157(a). This is the type of proceeding that a bankruptcy judge
17 may finally determine under 28 U.S.C. § 157(b)(2)(A) and (O).

18
19 II.

20 Pinnacle's motion to assume the Franchise Agreements is
21 governed by 11 U.S.C. § 365(a), which permits the trustee (or as
22 in this case the DIP) to "assume or reject any executory contract
23 or unexpired lease of the debtor," subject to certain exceptions
24 outlined elsewhere in § 365. Franchise agreements that are not
25 terminated pre-petition are almost universally deemed to be
26 executory contracts subject to assumption or rejection. *Sir*
27 *Speedy, Inc. v. Morse*, 256 B.R. 657, 659 (D. Mass. 2000). The
28 parties here agree that the Franchise Agreements fall within the

1 type of agreements that are subject to § 365 if none of the
2 exceptions preclude assumption.

3 Popeyes argues that Pinnacle cannot assume the Franchise
4 Agreements because of the operation of § 365(c)(1), which states:

5 (c) The [DIP] may not assume or assign any executory
6 contract or unexpired lease of the debtor, whether or
7 not such contract or lease prohibits or restricts
assignment of rights or delegation of duties, if—

8 (1)

9 (A) applicable law excuses a party, other than the
10 debtor, to such contract or lease from accepting
11 performance from or rendering performance to an entity
12 other than the debtor or the debtor in possession,
whether or not such contract or lease prohibits or
restricts assignment of rights or delegation of duties;
and

13 (B) such party does not consent to such assumption or
14 assignment[.]

15 11 U.S.C. § 365(c)(1). Or restated: a debtor may neither assume
16 nor assign a contract if applicable law excuses a counterparty to
17 the contract from accepting performance from or rendering
18 performance to any entity other than the debtor unless the
19 counterparty consents to such assumption and/or assignment.

20 While this language is seemingly straightforward, it has led
21 to two different theories of application: the “hypothetical test”
22 and the “actual test.” Under the “hypothetical test,” even if the
23 debtor merely wishes to assume an executory contract or an
24 unexpired lease and not assign its contract rights to a third
25 party, the counterparty may still withhold its consent and block
26 assumption if there is a hypothetical third party to whom the
27 debtor might assign its contract rights but as to whom the
28 counterparty would be excused from performing for under

1 applicable law. *In Re James Cable Partners*, 27 F.3d 534, 537
2 (11th Cir. 1994).¹ Under the “actual test,” the counterparty
3 would only be able to block assumption if there were an actual
4 third party to whom the counterparty would be forced to accept
5 performance other than the debtor with whom the counterparty had
6 contract. *Institut Pasteur v. Cambridge Biotech Corp.*, 104 F.3d
7 489, 493 (1st Cir. 1997).²

8 Proponents of the actual test argue that it better fulfills
9 the intent of Congress in enacting § 365(c)(1) and is consistent
10 with the Bankruptcy Code’s reorganization policy. Proponents of
11 the hypothetical test argue that it follows the actual written
12 text of § 365(c)(1) which, despite arguments to the contrary, is
13 unambiguous. *In re Catapult Entm’t*, 165 F.3d 747, 749
14 (summarizing actual and hypothetical tests and joining circuits
15 that apply the latter). As of this writing, it appears that the
16 majority of the circuit courts of appeals to have considered the
17 issue, including the Ninth Circuit, follow the hypothetical test
18 and interpret § 365(c) to mean that “where ‘applicable law’ bars
19 or excuses assignment of the underlying agreement, both
20 assumption and assignment are prohibited.” 3 Collier on
21 Bankruptcy § 365.07. See *Catapult*, 165 F.3d at 749. “Applicable
22 law” means any law applicable to the contract other than
23 bankruptcy law. *In Re XMH Corp.*, 647 F.3d 690, 695 (7th Cir.,
24 2011).

26 ¹ In addition to the Eleventh and Ninth, the Third and Fourth Circuits have
27 also adopted the “hypothetical test.” See, *In re Sunterra*, 361 F.2d 257 (4th
28 Cir. 2004); *In re W. Elec’s. Inc.*, 852 F.2d 79 (3rd Cir. 1998).

² The Fifth Circuit also follows the “actual test” view. *In re Mirant*, 440
F.3d 238 (5th Cir., 2006).

The court acknowledges that the hypothetical test often has devastating effects on the ability of Chapter 11 debtors to reorganize, especially when a debtor franchisee depends upon maintenance of the franchise for any kind of reorganization. As stated in *In re Cumberland Corral, LLC*:

In the present case, there is no dispute that the Franchise Agreements, by their terms, do not allow assignment without Golden Corral's consent. However, the Debtor has no intention of assigning the Franchise Agreements, and assumption would maintain the parties' relationship under the Franchise Agreements. In other words, allowing the Debtor to assume the Franchise Agreements is not forcing Golden Corral to accept performance from some unknown third party. Instead, assumption would maintain the parties' relationship under the Franchise Agreements.

Under these circumstances, the Court is persuaded by the reasoning of those courts that have adopted the actual test. To allow Golden Corral to block assumption of the Franchise Agreements because such agreements could not be assigned would allow Golden Corral a windfall while destroying the Debtor's chances at reorganization. Such an outcome would be contrary to the purposes of the Bankruptcy Code.

In re Cumberland Corral, LLC, No. 313-06325, 2014 Bankr. LEXIS 936, at *23-25 (Bankr. M.D. Tenn. Mar. 11, 2014).³

Unfortunately for Pinnacle, the Ninth Circuit has spoken to this issue unambiguously in *Catapult*, and the court is obligated to apply the hypothetical test to this case.

III.

Under the *Catapult* hypothetical test, Popeyes can effectively block Pinnacle from assuming the Franchise Agreements if it can show that applicable law would excuse Popeyes from

3 The Middle District of Tennessee is in the Sixth Circuit. The court has not
been directed to any circuit authority in the Sixth Circuit adopting either
the hypothetical or actual tests.

1 accepting performance from any hypothetical third party to whom
2 Pinnacle might theoretically assign its rights under the
3 Franchise Agreements post-assumption, regardless of the existence
4 of any actual such third party. Popeyes has consistently
5 maintained in this case that it will not consent to assumption by
6 Pinnacle effectively blocking Pinnacle's assumption of the
7 Franchise Agreements under § 365(c)(1)(A) and (B). Popeyes has
8 stated they have suggested to Pinnacle some approved successors
9 to Pinnacle's franchises.

10 The specific "applicable law" within the meaning of
11 § 365(c)(1) are the Lanham Act and CFRA. We will examine each.

12
13 A. The Lanham Act.

14 Popeyes argues that the Franchise Agreements all require use
15 of a trademark. Pinnacle concedes that. But the analysis of
16 whether the Lanham Act is an "applicable law" that preserves
17 Popeyes' right to refuse consent to Pinnacle's assumption
18 requires examination of the application of the Lanham Act in the
19 context of executory contract assumption.

20 Federal trademark law is governed by 15 U.S.C. §§ et
21 seq., referred to colloquially as "the Lanham Act."

22 Trademark rights are intangible property rights because
23 their primary feature and value are consumers'
24 perceptions of the mark. Trademarks are valuable
25 property rights that allow their owners to protect the
26 good will of their name and products by preventing
27 unwarranted interference and use of their mark by
28 others. As a grant of permission to use another's
mark, the trademark owner has a significant interest in
controlling to whom the mark is transferred because the
subsequent value of the trademark will be based
entirely on good will. Good will and trademarks "go
hand in hand, at least to the extent that an attempted
transfer of a trademark is void without transfer of the
good will associated with the trademark." Indeed, the

1 Lanham Act provides that "a registered mark...shall be
2 assignable with the good will of a business in which
3 the mark is used." The trademark owner not only has a
4 right to assign a trademark, but the same owner also
5 maintains a right and duty to control the quality of
6 goods sold under the mark. 15 U.S.C. § 1060. Because
7 the owner of the trademark has an interest in the party
8 to whom the trademark is assigned so that it can
9 maintain the good will, quality, and value of its
10 products and thereby its trademark, trademark rights
11 are personal to the assignee and not freely assignable
12 to a third party.

13 *N.C.P. Mktg. Grp. v. Blanks (In re N.C.P. Mktg. Grp.)*, 337
14 B.R. 230, 236 (D. Nev. 2005), *aff'd* 279 Fed. Appx. 561 (9th Cir.
15 2008), *cert. denied*, 556 U.S. 1145 (2009) (internal citations
16 omitted). See also *Miller v. Glenn Miller Productions*, 318
17 F.Supp.2d 923, 928 (C.D. Cal. 2004) (holding that trademark
18 licensors have an ownership interest in their marks that would be
19 "severely diminished if a licensee were allowed to sub-license
20 without the licensor's permission"); *XMH Corp.*, 647 F.3d at 695.
21 ("The universal rule is that trademark licenses are not
22 assignable in the absence of a clause in the contract expressly
23 authorizing the assignment.") J. Thomas McCarthy, 4 McCarthy on
24 Trademarks and Unfair Competition § 14.22 (4th ed. 2005) ("[S]ince
25 the licensor-trademark owner has the duty to control the quality
26 of goods sold under its mark, it must have the right to pass upon
27 the abilities of new potential licensees.")

28 1. *Pinnacle's Lanham Act Arguments.*

Pinnacle's arguments on the Lanham Act issue are minimal.
To the extent that the topic is addressed, Pinnacle appears to
suggest that CFRA trumps federal law on the issue of trademarks
as part of the bundle of rights conveyed through Franchise

1 Agreements and thus, by extension, trumps the plain language of
2 § 365(c)(1). Doc. #226 (Debtor's Motion at pg. 8); Doc. #260
3 (Debtor's Reply Brief at pg. 6). Pinnacle argues that assignment
4 of trademarks is primarily an issue of state law. That may be
5 true.⁴ Pinnacle's cited cases do not support its contention that
6 § 365(f) controls.

7 *In Orion Pictures Co. v. Showtime Networks (In re Orion*
8 *Pictures Co.)*, 4 F.3d 1095, 1098 (2d Cir. 1993) the issue before
9 the Second Circuit was whether the bankruptcy court erred in
10 resolving a disputed issue of fact between parties to a contract
11 in the context of deciding whether to grant a motion to assume
12 that contract. The question of whether the opposing party could
13 defeat the motion to assume altogether under § 365(c)(1) was not
14 an issue before the court.

15 Pinnacle cites *Georgia Ports Auth. V. Diamond Mfg. Co. (In*
16 *re Diamond Mfg. Co.)*, 164 B.R 189, 199 (Bankr. S.D. Ga. 1994) for
17 an explanation of how the burden of proof shifts in deciding
18 issues pertaining to a motion to assume or assign, with the
19 debtor bearing the initial burden of proof (1) that a contract is
20 subject to assumption and (2) that all § 365 requirements have
21 been met. If the debtor meets those requirements, the burden
22 shifts to non-debtor counterparty to provide evidence of defaults
23 and, upon doing so, back to the debtor to prove adequate "cure"
24 of those defaults. *Diamond Mfg. Co.* 164 B.R. at 199. However,
25 § 365(c)(1) was not an issue in that case and was not addressed
26 by the court.

27 _____
28 ⁴ The Lanham Act does not preempt all aspects of franchise law. See, 15 U.S.C.
§ 1127; *Marinello v. Shell Oil*, 511 F.2d 853 (3rd Cir. 1975).

1 Pinnacle also acknowledges the applicability of *Catapult* to
2 this motion but argues that it should be read “narrowly because
3 *Catapult* requires that ‘applicable law’ preclude assignment
4 before § 365(c)(1) applies.” Doc. 226. Pinnacle argues that the
5 only “applicable law” that is relevant to the court’s analysis is
6 CFRA which encourages assignment. *Id.*

7 Finally, in its reply brief, Pinnacle also cites *Tap*
8 *Publications, Inc. v. Chinese Yellow Pages*, (925 F.Supp. 212, 217
9 (S.D.N.Y. 1996)) for the proposition that “state contract law
10 governs the assignment of a trademark license.” Doc. #260. That
11 is, frankly, a misreading of the facts and holding of *Tap*
12 *Publications*. In that case, the plaintiff-corporation (“Tap”)
13 brought Lanham Act claims and other claims against a trademark
14 holder (“ASM”) under the theory that ASM had contractually given
15 a right to use the mark in question to a third party (“Key”), who
16 in turn transferred that right to Tap. *Tap Publ'ns*, 925 F. Supp.
17 at 215-16. The court held that Tap’s claims were not Lanham Act
18 claims but simply state contract law claims, because the question
19 of whether any trademark rights had been validly assigned was one
20 of contract interpretation, and the court concluded that no such
21 evidence of a valid assignment via contract existed. *Id.* at 218.

22 Though the court agrees with the general principle that the
23 validity of an assignment of trademark rights via contract is
24 typically a matter of state law contract interpretation, that is
25 irrelevant to the § 365(c)(1) analysis because, under the
26 hypothetical test, there is no contract between the debtor and
27 any third party to be considered, hence the use of the word
28 ///

1 "hypothetical." Indeed, elsewhere in *Tap Publications*, the court
2 notes that:

3 The right of a licensee to sub-license to others must
4 be determined by whether the license clearly grants
5 such a power. Similarly, the general rule is that
6 unless the license states otherwise, the licensee's
7 right to use the licensed mark is personal and cannot
8 be assigned to another.

9
10 Id. (citing 2 McCarthy on Trademarks and Unfair Competition
11 § 18.13[2] (3d ed. 1996)).

12
13 2. *Popeyes' Lanham Act Arguments.*

14 In response to Pinnacle, Popeyes' argues that, in the
15 context of Franchise Agreements and trademark licenses, the
16 "applicable law" which triggers § 365(c)(1)'s restriction on
17 assumption and assignment is the Lanham Act:

18 In particular, the Lanham Act provides that a
19 registrant of a mark registered in the Patent and
20 Trademark Office is entitled to nationwide trademark
21 protection. 15 U.S.C. § 1072. *In re The Travelot Co.*,
22 286 B.R. 447, 454-455 (Bankr. S.D. Ga. 2002). The
23 Lanham Act defines a trademark, in part, as "any word,
24 name, symbol, or device, or any combination thereof . .
25 . used by a person . . . to identify and distinguish
26 his or her goods, including a unique product, from
27 those manufactured or sold by others and to indicate
28 the source of the goods, even if that source is
unknown." 15 U.S.C. § 1127. Moreover, the Lanham Act
prevents the unauthorized use or transfer of a
federally registered trademark. For example, it: (a)
authorizes a registrant to sue and obtain injunctive
relief against the non-consensual use of trademark, 15
U.S.C. § 1116; (b) provides that "[a]ny person who
shall, without the consent of the registrant . . . use
in commerce any reproduction . . . of a registered mark
in connection with the sale . . . of any goods . . .
shall be liable in a civil action", 15 U.S.C. § 1114;
and (c) provides that "[a]ny person who . . . uses in
commerce any word, term, name, symbol, or device . . .
which . . . is likely to cause confusion, or to cause
mistake, or to deceive as to the affiliation,
connection, or association of such person with another
person, or as to the origin, sponsorship, or approval

1 of his or her goods, services or commercial activities
2 by another person . . . shall be liable in a civil
3 action" 15 U.S.C. § 1125.

4 Doc. #245 at n.7. Popeyes cites a number of cases which identify
5 the Lanham Act as the relevant "applicable law" that triggers
6 § 365(c)(1) in cases involving assumption of Franchise agreements
7 and trademark licenses, though only one of those cases, *In re*
8 *N.C.P. Mktg. Group Inc.*, 337 B.R. at 235-237 is a Ninth Circuit
9 case. (Nevada District Court extending reasoning of *Catapult* to
10 federal trademark claims). In that case, the court stated:

11 Indeed, the Lanham Act provides that "a registered
12 mark...shall be assignable with the good will of a
13 business in which the mark is used." The trademark
14 owner not only has a right to assign a trademark, but
15 the same owner also maintains a right and duty to
16 control the quality of goods sold under the mark. 15
17 U.S.C. § 1060 . Because the owner of the trademark has
18 an interest in the party to whom the trademark is
19 assigned so that it can maintain the good will,
20 quality, and value of its products and thereby its
21 trademark, trademark rights are personal to the
22 assignee and not freely assignable to a third party.
23 J. Thomas McCarthy, 4 McCarthy on Trademarks and Unfair
24 Competition § 25.33 (4th ed. 2005) ("since the
25 licensor-trademark owner has the duty to control the
26 quality of goods sold under its mark, it must have the
27 right to pass upon the abilities of new potential
28 licensees.").

21 Id. at 236. While there is no controlling authority in the Ninth
22 Circuit on the issue of applying federal trademark law as
23 "applicable law" in the context of § 365(c)(1), the court finds
24 *N.C.P. Mkt. Group* to be persuasive authority and finds that
25 Popeyes' rights under the Lanham Act represent "applicable law"
26 that excuses Popeyes from accepting performance from or rendering
27 performance to an entity other than Pinnacle under § 365(c)(1).
28 Thus, *Catapult* compels the conclusion that Pinnacle can neither

1 assign nor assume the Franchise agreements without Popeyes'
2 consent.

3
4 B. CFRA.

5 Pinnacle is largely reluctant to engage with the Lanham Act
6 because it insists that CFRA controls and, for a variety of
7 reasons, effectively trumps Popeyes' rights under § 365(c)(1) .
8 In its motion, Pinnacle argues that CFRA is the only "applicable
9 law" that matters and it encourages assignment. Doc. #226. The
10 relevant provisions of CFRA are found in § 20028(a)-(b):

11 (a) It is unlawful for a franchisor to prevent a
12 franchisee from selling or transferring a franchise,
13 all or substantially all of the assets of the franchise
14 business, or a controlling or noncontrolling interest
15 in the franchise business, to another person **provided**
16 **that the person is qualified under the franchisor's**
17 **then-existing standards for the approval of new or**
18 **renewing franchisees**, these standards to be made
19 available to the franchisee, as provided in Section
20 20029, and to be consistently applied to similarly
21 situated franchisees operating within the franchise
22 brand, and the franchisee and the buyer, transferee, or
23 assignee comply with the transfer conditions specified
24 in the franchise agreement.

25 (b) **Notwithstanding subdivision (a), a franchisee**
26 **shall not have the right to sell, transfer, or assign**
27 **the franchise, all or substantially all of the assets**
28 **of the franchise business, or a controlling or**
29 **noncontrolling interest in the franchise business,**
30 **without the written consent of the franchisor, except**
31 **that the consent shall not be withheld unless the**
32 **buyer, transferee, or assignee does not meet the**
33 **standards for new or renewing franchisees described in**
34 **subdivision (a) or the franchisee and the buyer,**
35 **transferee, or assignee do not comply with the transfer**
36 **conditions specified in the franchise agreement.**

37 Cal. Bus. & Prof. Code § 20028 *emphasis added*. Pinnacle
38 interprets this language as follows:

39 The statute provides that the franchise is
40 transferrable and assignable to a proper transferee
41 over the objection of a franchisor as a matter of state

1 law and that under such circumstances, transfer or
2 assignment may be compelled by a court. The statute
3 provides that it is unlawful for the franchisor to
4 prevent such a transfer or assignment; accordingly,
5 there is a limitation on assignability or sale, but no
6 prohibition as required by Section 365(c)(1).

7 Doc. #171 (Debtor's Opposition to Popeyes' Motion to Remove
8 Debtor from Possession, incorporated by reference in Doc. #226).

9 Unsurprisingly, Popeyes disagrees with Pinnacle's
10 interpretation of CFRA. Doc. #245. Reading the same statutory
11 language as quoted above, Popeyes interprets it to mean that

12 [w]hile CFRA provides that a franchisor cannot reject a
13 sale or transfer of a franchise agreement provided that
14 the proposed buyer otherwise qualifies under its
15 standards and meets other requirements, the statute is
16 equally clear that a franchisor can reject any such
17 proposed sale or transfer if the buyer does not qualify
18 under its standards.⁵

19 Id. Because the hypothetical test looks to the existence of a
20 hypothetical assignee to the Franchise Agreements for which
21 Popeyes would be excused from either accepting or rendering
22 performance under the Franchise Agreements, that necessarily
23 includes hypothetical assignees who do not qualify under Popeyes'
24 standards for approval of new or renewing franchises. Thus,
25 Popeyes argues, Pinnacle fails the hypothetical test under CFRA
26 as well.

27 ⁵ Popeyes also argues that since the relevant provisions of CFRA were adopted
28 by the California legislature and signed by the governor in 2015 and effective
January 1, 2016, the provisions of CFRA do not apply. Popeyes theory is all
but two of the franchise contracts between Popeyes and Pinnacle were entered
into before 2016. Pinnacle's predecessor entered into those contracts in
2013. The court rejects the argument. True enough, 2015 amendments effective
January 1, 2016 do apply only to agreements entered into or renewed on or
after January 1, 2016. Cal. Bus. & Prof. Code § 20041(b). The pre-2016
contracts were "assigned" to Pinnacle. New contracts were not entered into.
But under Cal. Bus. & Prof. Code § 20010 (in effect since January 1981) any
condition, stipulation or provision purporting to bind any person to waive
compliance with any provision of [CFRA] is contrary to public policy and void.

1 The parties also make much of a semantic distinction.
2 Pinnacle argues that *Catapult* must be read narrowly in light of
3 CFRA and the court must find that the applicable law “precludes”
4 assignment before § 365(c)(1) applies. Doc. #226. Popeyes’
5 objects to the idea that the applicable law must “preclude”
6 assignment and notes that the Code merely says that the
7 applicable law must “excuse” Popeyes from accepting or rendering
8 performance. Doc. #245. The court finds this distinction to be
9 of little importance. Under § 365(c)(1), assignment may be
10 “precluded” whenever the applicable law “excuses” performance and
11 the counterparty does not consent to assignment.

12 At oral argument, Pinnacle’s counsel stressed one passage of
13 *Catapult* as being dispositive of the issue here. The *Catapult*
14 court recognized the difficulty reconciling 11 U.S.C. § 365(f)(1)
15 and (2), “superiority” to any applicable law’s prohibitions,
16 restrictions, or conditions on a contract assignment and noted
17 that a trustee (or DIP as here) may assign the contract if it is
18 assumed and adequate assurance of future performance is provided.
19 165 F.3d at 751-52. The court reconciled the exception to this
20 broad rule under § 365(c)(1) by explaining:

21 Only if the law prohibits assignment on the rationale
22 that the identity of the contracting party is material
23 to the agreement will subsection (c)(1) rescue it.

24 *Catapult*, 165 F.3d at 751-52.

25 One case cited by Pinnacle’s counsel in argument was cited
26 by the Ninth Circuit as supporting the above. *In re Antonelli*,
27 148 B.R. 443, 448 (D. Md. 1992). On an appeal from the
28 bankruptcy court order confirming a Chapter 11 Plan, the district
court there affirmed the bankruptcy court. *Id.* at 450.

1 Appellants who were partners of Antonelli argued that § 365(c)
2 precluded confirmation because under controlling Maryland
3 Partnership Law, the assignment of a partner's interest does not
4 give the assignee any more rights than the value of the
5 partnership interest. The plan in *Antonelli* required Antonelli's
6 partnership decisions to be screened by a post-confirmation
7 liquidation committee. There, the District Court framed the
8 issue as: "the non-debtor party to a contract is excused from
9 performance if the identity of the debtor is a material condition
10 of the contract when considered in the context of the obligations
11 which remain to be performed under the contract." *Id.* at 448.

12 The *Antonelli* court then went on to analyze the practical
13 facts before it in that case. *Id.* at 449. The partnerships
14 involved there were mature real estate ventures with little
15 active partner participation required and a property manager for
16 the properties was handling day-to-day decisions. *Id.* The court
17 noted certain partnerships may be at a stage where a partner's
18 identity is more important. *Id.* at 449. The *Antonelli* court
19 mentioned the bankruptcy court's finding about the liquidating
20 committee's interests and concluded that the adequate assurance
21 of future performance required by § 365(f)(2)(B) were satisfied.
22 *Id.* at 450.

23 A franchisor such as Popeyes here, has rigorous standards
24 that a potential franchisee must meet before being awarded a
25 franchise. By definition, then, the identity of the franchisee
26 is material to the franchise contract. The franchises here are
27 ongoing quick service restaurants in two metropolitan locations.
28 A franchisor's standards and requirements are material to the

1 franchise. Thus, here the exception of § 365(c) to the general
2 permissible assignments under § 365(f) apply. *Catapult*.
3 Applicable law excuses Popeyes from accepting performance from a
4 party other than the Debtor. The identity of a franchisee is
5 material to the franchise contract so the contracts here are
6 “rescued” under § 365(c).

7 Pinnacle directs the court’s attention to *In re Van Ness*
8 *Auto Plaza, Inc.*, 120 B.R. 545 (Bankr. N.D. Cal. 1990) which
9 Pinnacle concedes is both a pre-*Catapult* and a pre-CFRA case.
10 Doc. #260. In that case, the bankruptcy judge noted that, under
11 California state law as it existed at the time, a counterparty
12 under § 365(c)(1) could not “unreasonably” withhold consent. *Van*
13 *Ness*, 120 B.R. at 546. The court went on to find that the
14 counterparty (Porsche) reasonably withheld consent to the
15 transfer. *Id.*

16 *Van Ness* is not controlling here. The relevant law in *Van*
17 *Ness* was the California Vehicle Code, and the franchise to be
18 assigned was a Porsche dealership. *Id.* The circumstances of
19 potentially assigning an auto dealership are qualitatively
20 different than assigning a franchise in a nationally-recognized
21 fast food restaurant with its own trademarks, distinctive trade
22 dress, and goodwill. More importantly, in *Van Ness*, there was an
23 actual assignee involved, and Porsche could point to specific
24 grounds why its refusal to consent to the assignment was
25 reasonable. In other words, the operation of the Ninth Circuit’s
26 hypothetical test was avoided completely.

27 Finally, Popeyes cites to the only case that the court is
28 aware interprets CFRA (or at least § 20028(b)) since this fairly

1 new statute was enacted: *Prieto Auto., Inc. v. Volvo Car USA, LLC*
2 (*"Prieto"*), No. 1:21-cv-01085-KES-EPG, 2024 U.S. Dist. LEXIS
3 106230, at *34 (E.D. Cal. June 13, 2024). While the facts are
4 rather different (another car dealership) and the case was not a
5 bankruptcy case which implicated § 365(c)(1), the *Prieto* court
6 stated that CFRA "makes clear that a franchisee 'shall not have
7 the right to sell' the franchise without the franchisor's written
8 consent . *Prieto*, No. 1:21-cv-01085-KES-EPG, 2024 U.S. Dist.
9 LEXIS 106230, at *33. Because of the posture of the *Prieto* case,
10 the issue of whether any denial of consent must be reasonable was
11 not before the court.

12 The court agrees with Popeyes' analysis of CFRA and its
13 implications for § 365(c)(1). Regardless of whether CFRA favors
14 transfer or assignability of franchises, the relevant question in
15 this case is the one raised by *Catapult*: Is there a hypothetical
16 third party to whom Pinnacle might be excused from accepting or
17 rendering performance because such a hypothetical third party
18 might not qualify for Popeyes standards for approval under CFRA?
19 The answer is yes. Accordingly, CFRA provides alternative
20 grounds for concluding that Pinnacle fails the *Catapult*
21 hypothetical test and cannot assume the Franchise Agreements if
22 Popeyes continues to withhold consent.

23 24 CONCLUSION

25 Based on the foregoing analysis, the court finds that
26 Pinnacle has failed to meet its burden under the *Catapult*
27 hypothetical test. Accordingly, the motion to assume the
28 Franchise Agreements must be **DENIED**.

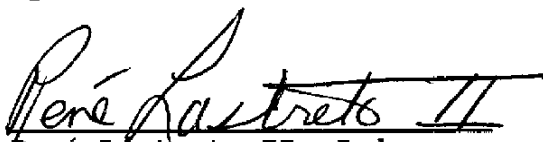
1 The court is cognizant of the fact that this interpretation
2 of the hypothetical test in the context of franchise agreements
3 may present serious difficulties for franchisees who wish to
4 reorganize under bankruptcy law. After all, the court expects
5 that, for most franchisee business, the franchise agreements are
6 the business. Accordingly, the application of the hypothetical
7 test, in many situations, may give veto power over the
8 possibility of effective reorganization to the franchisor, who
9 may also be a hostile creditor. Unfortunately, *dura lex sed lex*
10 -- The law is hard, but it is the law.

11 The court notes that Popeyes has submitted additional
12 grounds for denying the motion based on what it purports to be
13 "incurable non-monetary defaults" and monetary defaults on the
14 part of Pinnacle. Because these are fact-intensive, the court
15 declines to consider them in light of the gateway application of
16 the *Catapult* test.

17 A separate order will issue.

18
19 **Dated:** Oct 10, 2024

By the Court

20
21 
22 René Lastreto II, Judge
23 United States Bankruptcy Court
24
25
26
27
28

**Instructions to Clerk of Court
Service List - Not Part of Order/Judgment**

The Clerk of Court is instructed to send the Order/Judgment or other court generated document transmitted herewith to the parties below. The Clerk of Court will send the Order via the BNC or, if checked ____, via the U.S. mail.

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